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Letter dated 18 July 2000 from the Permanent Representative of Maldives to the United Nations addressed to the President of the Economic and Social Council

I have the honour to forward herewith a letter dated 13 July 2000 addressed to you from Mr. Fathulla Jameel, Minister of Foreign Affairs of the Republic of Maldives, regarding the recommendation of the Committee for Development Policy to graduate Maldives from the list of the least developed countries (see annex).

I should be most grateful if you would kindly bring the present letter and its annex to the attention of the members of the Economic and Social Council and circulate it as an official document of the Council under agenda item 13 (a).

(*Signed*) Hussain **Shihab**
Permanent Representative

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Annex to the letter dated 18 July 2000 from the Permanent Representative of Maldives to the United Nations addressed to the President of the Economic and Social Council

I have the honour to refer to the decision of the Committee for Development Policy during its second session, in April 2000, to recommend to the Economic and Social Council that Maldives be graduated from the list of the least developed countries with immediate effect. The recommendation is to be considered at the current session of the Council.

I am forwarding herewith a document prepared by my Government clarifying the position of Maldives in this matter and highlighting the serious ramifications of the course of action recommended by the Committee for Development Policy. We are of the opinion that while we have made some progress in our socio-economic development efforts, there are numerous circumstances and constraints that are peculiar to Maldives that warrant our continued access to the preferential treatment available to the least developed countries. We are convinced that graduation would not only make our current development status unsustainable but would also cause our socio-economic situation to deteriorate.

I would appreciate it if you could bring these matters to the attention of the members of the Economic and Social Council when the question of graduation of the Maldives is being considered.

(*Signed*) Fathulla **Jameel**

Enclosure

Memorandum containing observations and comments of the Government of the Republic of Maldives on the recommendation by the Committee for Development Policy to graduate the Maldives from the list of the least developed countries

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A- Critical factors not captured by the indicators used

The recommendation contained in the Report of the CDP on its Second Session is unjustified because the CDP's assessment ignores critical characteristics of the Maldives' development status and does not address or give adequate attention to a number of vital issues. The CDP's report cannot, therefore, be considered valid for the Maldives. For example:

1. Indicators used have not captured the extent of poverty and the level of regional disparities, nor have they been sensitive enough to the special circumstances of the Maldives that impose severe structural constraints to development. At the same time, the indicators have failed to highlight the lack of opportunity for economic diversification and the intensity of the vulnerability the country faces.

2. GDP per capita figure conceals the extent of poverty and income disparities in the Maldives. For example, one in four of all Maldivians live on incomes below the World Bank's poverty line of $1 per day; and 43% of the population live on less than $1.25 per day. The average income of 75% of the total population is merely $1.60 per day, in a situation where nearly all food and other basic items are imported, and distribution costs are high. In fact, according to the UNDP's Human Development Report 2000, the Maldives is the 7th worst country in the world in terms of malnutrition[1].

3. The use of per capita GDP is misleading because the GNP is significantly smaller than the GDP due to high dependence on imported labour and repatriation of profits. The per capita income in the rural atolls ($584) is less than one-half of the crude aggregate of per capita GDP. Similar disparities exist in access to basic services such as education, health care, water and sanitation and electricity. Such regional disparities exist because of severe structural constraints relating to the geo-physical layout of the country, the narrow economic base and the small size of the populations in the rural atolls. Collectively these features impede re-distributive policies and developmental efforts despite extensive and continuous programmes aimed at the development of the rural atolls.

4. The CDP looked at infant mortality rates although it had acknowledged that child (under 5) mortality is a better indicator for health status. The WHO ranking for child survival for the Maldives is 134th out of the 191 member states of WHO. All the threshold countries were ranked higher than the Maldives reflecting their better health status: Samoa 81st, Cape Verde 123rd

[1] UNDP, Human Development Report 2000, pp. 169-70, Table 4.

and Vanuatu 127th[2]. According to WHO data, child (under 5) mortality is 90 per thousand for males and 86 per thousand for females in the Maldives. These figures are also the highest mortality rates for the threshold countries: Samoa - 28 for males and 25 fc males; Cape Verde - 55 for males and 50 for females; and Vanuatu 64 for males and 57 for females.[3] This is notwithstanding the fact that at US$248.00 the Maldives has the highest per capita health expenditure (Samoa $108.00, Cape Verde $60.00 and Vanuatu $85.00,)[4]. Total expenditure on health as a percentage of GDP is 8.2% for the Maldives, 3.8% for Samoa, 3.3% for Vanuatu and 2.8% for Cape Verde.[5]

5. Although the Maldives is ranked 89 in the UNDP's Human Development Index, the UNDP's own Human Poverty Index shows that the extent of poverty in the Maldives is worse than deprivation in the next ten developing countries which follow the Maldives in the HDI ranking.[6]

6. The island structure of the Maldives, where the population is spread over 200 small islands (many of which become inaccessible for days during regular rough seas in monsoons), makes the constraints of the sea transportation system the most critical handicap to production and delivery of services. This is comparable to a total lack of feeder roads and railways between urban and rural areas in other countries.

   Additionally, transportation in the Maldives is constrained by the lack of port and harbour facilities and high costs. The low levels of consumption and production of the small island populations in fact restrict the development of a regular cost-efficient transport system. Inter-island transport is compounded by the strong currents that flow between the atolls, the dangerous reef entrances and the shallow waters of the lagoons. The lack of sea transport infrastructure leads to a pervasive multiplier effect constraining the entire economy in the Maldives.

7. Similar problems afflict other sectors of the economy. For example, in the Maldives, investment costs in telecommunications are disproportionately high. The distances that separate the atolls cannot be bridged by conventional microwave technology, leaving the nation no alternative but to make use of more expensive satellite technology.

8. The indicators do not capture the extensive constraints to human resource development and the dependence of human resource development programmes on aid. The dispersal of population over 200 islands, 90% of which have less than 1,000 inhabitants, imposes very high unit costs and diseconomies of scale in the provision of infrastructure for human resource development. The average construction cost of a primary school or a small

[2] WHO, The World Health Report 2000, pp. 177-183, Table 5.

[3] *Ibid.*, pp. 156-159, Table 2.

[4] *Ibid.* pp. 192-195, Table 8.

[5] Ibid.

[6] UNDP, Human Development Report 2000, pp. 169-70.

clinic on an island in the Maldives is five-six times higher than the cost of a comparable school in its South Asian island neighbour, Sri Lanka. The national burden is further magnified by the need for extensive replication of all services in each of the 200 islands due to the small size and insularity of these islands. This burden is far more severe than those experienced by land-locked small states, which can make use of the infrastructure and services of larger neighbouring countries.

Development efforts and prospects are severely constrained by low level of human resource development. This is evident in the fact that technical assistance consumes over 50% of foreign aid. Any decline in foreign technical assistance would seriously impair the programs in capacity building and institutional development

9. Lack of diversification and high vulnerability of the economy are areas of acute concern that justifies the continuation of preferences granted to LDCs. The narrowness of the economic base is evident from the excessive dependence on the single sector – tourism. It is estimated that gross income from tourism amounts to 84% of the GDP in recent years. Crises in the fisheries sector have increased dependence on the tourism industry, while low technology base, low levels of human resource development, high factor outlays necessitated by small scale, wide geographic dispersal and costs related to international and domestic transport have restricted opportunities for diversification. Dependence on imported raw materials further handicaps efforts to diversify.

10. The prospects for diversification of the Maldivian economy are relatively low given the associated high costs. Lacking both natural and human resources, the Maldives depends on imported raw materials and expatriate labour for the production of goods and services. Added to this are the high costs associated with transportation of the finished product to the various markets abroad, largely as a result of insufficient return cargo. For example, a 20ft container from the Maldives to a north European port is about US$1,500-1,700 compared to about US$600 from Bangkok. A similar cost difference is evident in-bound freight from its main source of imports, Singapore. While, the cost of shipping a standard container from the USA to Sri Lanka is in the order of US$600 the freight costs from Singapore to the Maldives, which is only a fraction of that distance, is nearly three times higher.

11. The high vulnerability of the economy to various shocks is itself encapsulated by the wide fluctuations registered by the Maldives in the scores recorded by the CDP for the country's economy since the EDI/EVI has been calculated. CDP scores for the Maldives on the EDI/EVI have fluctuated between 18.0 (in 1991), 11.0 (in 1994), 30.5 (in 1997), and 32.2 (in 2000).

12. Ecological vulnerability is not only a source of long-term threat. In the recent past, the Maldives has been severely affected on numerous occasions by extreme weather conditions that acquired the character of natural disasters. On one occasion, the damage was estimated at 22% of GDP. Moreover, the continuous exposure to such ecological hazards as coastal erosion and storm

surges is imposing a huge drain on available resources, including foreign aid. In the immediate aftermath of storm surges in 1987, the expenditure required for preventive measures exceeded $70 million dollars. Even at present, up to 90% of all inhabited islands suffer from coastal erosion. Some islands are seriously affected with the loss of not only the shoreline and vegetation but also houses and social infrastructure, compelling the Government to undertake urgent and costly resettlement programmes.

The necessity of adjustment to environmental threats imposes pressure to divert funds from essential socio-economic services to critical environmental protection measures, and, therefore, the opportunity costs of environmental programmes on social services are immense.

13. In many islands, groundwater supplies have been exhausted, are saline or contaminated, and populations are dependent upon rainwater, which is insufficient to meet even the basic daily requirements. Addressing this rapidly deteriorating situation requires continued donor assistance in complementing the government's efforts to provide basic services to the rural population.

14. The CDP's assessment did not consider the country's limited capacity to sustain its current level of development. The achievements made by the Maldives, in terms of its development indicators, cannot be maintained if aid programmes are withdrawn. The level of social and economic development is very highly dependent on external aid. Foreign aid constitutes over 17% of GDP, and 60% public investments. This dependence is accentuated by the low level of competitiveness in attracting FDI and the inability to borrow commercially - factors which constrain the country's flexibility to adjust to a decline in the level of aid.

A comparison of FDI flows to the four marginal countries in 1997 shows Maldives in the most vulnerable position[7]:

Vanuatu	$30.3 million
Samoa	$20.0 million
Cape Verde	$11.6 million
Maldives	$ 7.7 million (the highest ever recorded for the country)

15. The implications on the country from the loss of benefits of being an LDC were not considered. Due to high factor costs and diseconomies of scale, the Maldives is able to compete in international markets purely on the basis of preferential access available to LDCs. Thus, erosion of preferential access to markets will cripple the economy. For example, the tuna industry, which is the largest employer, will collapse due to the loss of preferential access to the EU market. At the present time even with a 24 percent tariff concession in the EU market, the Maldives is barely able to survive the competition. The loss of preferential access will have a similar impact on the garment industry. Moreover, options for the expansion of foreign trade, such as through the South Asian Preferential Trading Arrangement, will also be diminished.

[7] UNCTAD, The Least Development Countries 1999 Report, United Nations, Geneva, 1999, Table 12, p. 45.

The loss of concessions eligible to LDCs, given the small size of the economy, will impose an unbearable debt burden on the country, slowing the overall rate of economic growth and leading to macroeconomic instability. More than 80% of total capital expenditure on socio-economic services and 60% of total development expenditure are from concessional loans and grant assistance. Over 17% of GDP comprise foreign aid. Although the aid to GDP ratio of 17% may be comparatively small, the threat of declining assistance levels must be considered in conjunction with the constraints on attracting FDI, which remains at a very low level, the size of the current account deficit (15% GDP in 1999), and the extent and nature of the developmental challenges facing the country.

B- Key issues overlooked by the Draft Vulnerability Profile

It is appreciated that ECOSOC decided to draw up country specific Vulnerability Profiles to qualitatively crosscheck the results of the quantitative assessment. However, in the case of the Maldives, the Vulnerability Profile is as yet seriously insufficient in comprehensively addressing the omissions and shortcomings of the quantitative criteria. In fact, the draft Profile exacerbated the misrepresentation of the actual situation of the Maldives. Listed below are some of the vital aspects overlooked by the Profile on several of the measures that were qualitatively assessed. The section below follows the structure of the Summary Profile.

1. Income Criterion

1.1 GNP/GDP per capita

Although the Maldives has *prima facie* exceeded the graduation threshold by GDP, it must be noted that in the case of Maldives the GNP is significantly lower than the GDP. The GNP figure given in the summary profile is highly questionable. 20% of GDP goes to non-Maldivians. The deficit in net private transfers has increased throughout the 1990s, from US$22 million in 1994 to US$32.5 million in 1996. Thus the per capita GNP is likely to be well below the graduation threshold.

1.2 Income distribution

Income difference between Male' and the atolls is much greater than stated in the report – one in four of all Maldivians live on incomes less than $1 per day or below the World Bank's definition of poverty. 43% of the population live on less than $1.25 per day.

2. Human Resource Criterion

While the indicators used highlight some of the areas of success for the Maldives they do not present an adequate assessment of the actual situation.

2.1 Primary and secondary school enrolment ratio

Although primary school enrolment is high, not all school children complete primary school, and only 50% of the relevant age group is enrolled in secondary school. This is a reflection of the inherent structural problems of

smallness of island populations, accessibility problems and problems associated with fragmentation of the population over vast distances.

2.2 Nutrition

Though calorie intake may be high, under-nourishment is high (49%) in the rural atolls. Nearly all food items are imported and expensive. Close to 50% of all children suffer from stunting and wasting due to poor nutrition.

3. Vulnerability Criterion – External Shocks

3.1 Natural shocks

The profile used by CDP focuses on long-term threats while ignoring natural shocks experienced regularly.

3.2 Economic shocks

The chronic vulnerability of the economy is understated in the Report. For the last thirty years the Maldives has experienced a series of external shocks which have affected critical sectors of the economy.

Fisheries, the nation's only merchandise trade export crashed due to a protectionist ban by the market in the 1970s. In the 1990s, fisheries continued to suffer repeated crises due to fluctuations in the world market. Export revenues from fisheries were reduced by one-fourth in the early 1990s, and revenues further plummeted by 50% in the mid-1990s and has again declined sharply since 1998.

The tourism sector has similarly been susceptible to unpredictable negative developments such as recession in markets, conflict in the region and elsewhere (Sri Lanka and the Gulf War) and negative publicity relating to coral bleaching and threat of sea level rise.

3.3 Instability of production

Assessment of instability of production through its focus on agriculture and manufacturing is inappropriate for the Maldives. Crop cultivation is limited due to non-availability of arable land, and production is frequently affected by salt water intrusion through storm surges. Exposure to shocks is also highly evident in the fisheries sector, which is subject to climatic changes and the *El Nino* phenomenon. Moreover, given the dominance of tourism in the economy, the CDP should have looked at an indicator, which takes into consideration the vulnerability of this sector.

3.4 Instability of exports of goods and services

The statement that the country experiences only "limited instability" of exports of goods and services is inaccurate.

Fluctuation in fisheries exports is not noted. Volatility of investment, low retention value of income, and dependence on preferential access to markets in the garment industry are not considered. The high risk of dependence on tourism and the narrow market concentration of the sector are not taken into account.

4. *Vulnerability Criterion – Exposure to Shocks*

4.1 Balance of payments

Exposure of balance of payments to risks of instability in fisheries and tourism earnings is understated. Income from receipts from tourism is equivalent to 84% of GDP. 28% of government revenue is derived directly from tourism. Dependence on foreign aid (30% of government revenue) is not stated.

4.2 Income

The very high risk of serious income shortfalls because of high dependence on tourism is not stated.

4.3 Economic concentration

The statement that high economic concentration has not so far been a factor of vulnerability is incorrect. The crisis in fisheries sector has had far reaching negative impacts on the economy, especially on rural employment.

Single sector dominance (as a percentage of total exports) among the four marginal countries, reviewed by the CDP, is greatest in the Maldives[8]:

Maldives	Travel:	68.4%
Samoa	Travel:	47.7%
Vanuatu	Travel:	40.9%
Cape Verde	Air Transport:	26.8%

4.4 Economic specialization

Though the emergence of tourism as a dominant economic sector had initially offset instability in the fisheries sector, the subsequent over-dependence on tourism has, in fact, contrary to the Vulnerability Profile, increased the exposure to high economic instability.

4.5 Employment

Risk of departure of expatriates is not the only shock that may impact on employment. Weakness in the fisheries sector has serious consequences on rural employment. There is high exposure of employment to the risk of instability or decline in aid, considering the volume of jobs directly linked to the large number of aid-funded infrastructure development programmes. Low levels of human resource development impose continued dependence on expatriates.

4.6 Social Status

Geographic dispersal, inaccessibility, high unit costs, poor socio-economic infrastructure and lack of resources make social status still highly dependent on continued foreign aid. More than 80% of total capital expenditure on socio-economic services are from concessional loans and grant assistance.

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[8] UNCTAD, The Least Development Countries 1999 Report, United Nations, Geneva, 1999, Table 19, pp. 87-89.

4.7 *Environment*

The Vulnerability Profile only focuses on natural disasters and long-term threats. It understates the high vulnerability of the Maldives even to regular natural phenomena such as storm surges and coral bleaching, and man-made disasters such as oil spills. Adverse weather conditions, which are frequent, heighten inaccessibility of the islands, disrupting the economy and increasing exposure to shocks.

5. ***Vulnerability Criterion – Resilience to Shocks***

5.1 *Structural factors*

Contrary to the Vulnerability Profile, smallness and remoteness of the islands impose structural constraints on the entire economy, including tourism. Small domestic market, diseconomies of scale, high infrastructure and transport costs, lack of competitiveness, economic inefficiency, constraints on mobility of domestic labour and high costs of human resource development are handicaps for socio-economic development

Geophysical features, dispersal of population, low resource base and high economic concentration are major structural impediments to resilience to shocks.

5.2 *Policy factors*

The Vulnerability Profile's assessment of relevant policy factors does not highlight the dependence on continued assistance for sustaining current development and the inability to adjust to a decline in the level of assistance.

6. ***Global Assessment***

The Vulnerability Profile's global assessment needs to be adjusted in view of the above. The Maldives suffers from great economic disadvantages, great exposure to short-term external shocks, and high dependence on foreign aid, in addition to vulnerability to environmental factors.

C. Inadequacy of the weight given to given to vulnerability

Despite the importance given by the UN General Assembly to the issue of vulnerability, the CDP has recommended graduation of the Maldives even though the country does not qualify on the EVI index. Vulnerability is a crucial factor in determining the constraints affecting the development status and prospects of LDCs, especially small island states. It has an overriding negating effect on achievements highlighted by the income criterion and the human development criterion.

Moreover, the CDP's recommendation that ECOSOC consider what special assistance could be given to the Maldives in response to its exceptional situation (para 99 of the Report) was not highlighted in its recommendation to graduate the Maldives on the basis of the country meeting the technical criteria for exclusion from the list of LDCs. The cautious approach taken by the CDP itself warrants the importance of deferring the graduation of the Maldives until the ECOSOC has been able to identify a suitable manner and appropriate measures

through which the international community may respond to the special circumstances of the Maldives.

D- Costs to the Maldives of graduation from LDC category

1. ***Loss of preferential access to markets:***

- Tuna exports to EU, the major market, will be affected with the imposition of a 24% tariff. At present, even without the tariff, the Maldives is barely able to compete with its main rivals due to high unit costs and diseconomies of scale.

- The garment industry will be shut down as at present exports rely on preferential access to the US market granted to the Maldives as an LDC.

2. ***Decline in foreign aid:***

- Even at present, many donors are citing assessments made in previous CDP reports and are reducing levels of assistance. Graduation will result in further decline that would severely affect the country's ability to sustain development programmes or even to maintain the current level of development.

- 60% of total development expenditure is derived from foreign aid (grants and concessional loans).

- 80% percent of total expenditure on socio-economic services is derived from foreign aid.

- Decline in aid will lead to serious unemployment problems given the volume of jobs directly linked to the large number of aid-funded infrastructure development programmes.

- High factor unit costs, diseconomies and narrow resource base limit flow of FDI. The level of FDI the Maldives has been able to attract is significantly smaller than those of the other threshold countries. (Moreover, with the loss of GSP access, one of the main draw-cards for FDI will be lost).

3. ***Increased debt burden:***

- Acceleration of past debt obligation resulting in increased debt-servicing burden. Repayment instalments under all IDA, ADB and NDF loans (87% of total debt as at end 1999) will increase by 100% of the amount of each maturity due thereafter.

- The loss of concessions will also lead to macro-economic instability, especially as the current account deficit stands at 15% of GDP (1999).

4. ***Loss of access to other special arrangements:***

- This includes loss of access to numerous technical assistance programmes when 50% of current aid is in the form of TA's designed to enhance human resource

capacity building. Other arrangements that will be denied are special and differential treatment under WTO and special programmes devoted to LDCs by IMO, ITU, UNESCO, UNCTAD and other multilateral organisations as well as bilateral donors. Similarly, access to multilateral negotiating forums will also be severely affected due to loss of assistance currently given to LDCs to facilitate their participation.